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Eligibility for CGT Small Business Relief – Not So Basic When It Comes to Shares and Trust Interests – February 2024

With:

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Information provided is general in nature; precise application depends on specific circumstances

Overview

- See paper for more detail and references
- Overview of additional requirements for accessing SBCGT concessions where CGT asset are trust/company interests
- Rationale for inclusion of some of the requirements
- CGT concession stakeholder test
- Active asset test where CGT asset are trust/company interests
- Modified active asset test
- Additional condition relating to taxpayer
- Additional condition relating to Object Entity

Terminology

- Taxpayer – person selling the share/trust interest
- Object Entity – company/trust whose shares are being sold
- Later entity – company/trust whose share/trust interest held by Object Entity
- MNAV test - $6million maximum net asset value test (considered in separate session)
- Turnover test – test for an entity to be considered a small business entity, noting aggregated turnover less than $2million due to modification in legislation (considered in separate session)
- Active asset test – test to determine if CGT asset sold is 'active' for the purposes of accessing the SBCGT concessions (considered in separate session)
- ITAA 1997 – *Income Tax Assessment Act 1997* (Cth)

Additional basic conditions

- Section 152-10(2) ITAA 1997 summarised to read:
  - (a) the **modified active asset test** – whereby 'CGT asset would still satisfy the active asset test…if the assumptions in subsection (2A) were made';
  - (b) **additional condition relating to taxpayer** – the taxpayer either needs to satisfy the maximum net asset value (MNAV) test or be carrying on a business just before the CGT event;
  - (c) **additional condition relating to Object Entity** – the Object Entity must satisfy either the MNAV test or is considered a CGT small business entity where:
    - (i) 'the only CGT assets or annual turnovers considered were those of the object entity, each affiliate of the object entity, and each entity controlled by the object entity in a way described in section 328- 125;
    - (ii) each reference in section 328- 125 to 40% were a reference to 20%; and
    - (iii) no determination under subsection 328-125(6) were in force;'

Additional basic conditions

- Section 152-10(2) ITAA 1997 summarised to read (cont):
  - (d) **CGT concession stakeholder test** – where just before the CGT event, either:
    - (i) the taxpayer was a CGT concession stakeholder in the object entity; or
    - (ii) CGT concession stakeholders in the object entity together have a small business participation percentage in the taxpayer of at least 90%.
- Originally additional basic conditions only required meeting the **CGT concession stakeholder test**
- Changes introduced in 2018 increased additional conditions to include:
  - **Modified active asset test**
  - **Additional condition relating to taxpayer**
  - **Additional condition relating to Object Entity**

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Additional basic conditions

- To understand how the newer additional basic conditions are to operate – useful to consider legislative guidance (e.g. rationale for such changes noted in the budget notes and explanatory memorandum):

  "The concessions assist owners of small businesses by providing relief from CGT on assets related to their business which helps them to re-invest and grow, as well as contribute to their retirement savings through the sale of the business. ***However, some taxpayers are able to access these concessions for assets which are unrelated to their small business, for instance through arranging their affairs so that their ownership interests in larger businesses do not count towards the tests for determining eligibility for the concessions****. …*

  This measure will improve the integrity of the tax system and ensure that these concessions are appropriately targeted."

  - 2017 Budget papers

Rationale for modified active asset test

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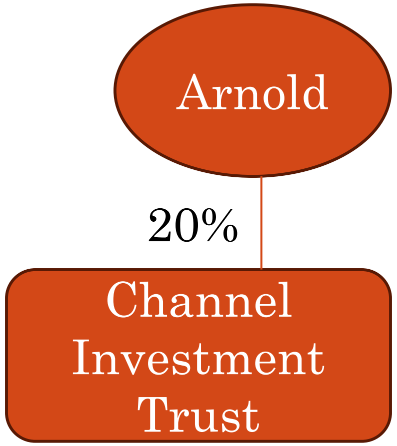
- Complicated rerun of the active asset test but the requirement notes that:

  "the active asset test in section 152-35 is modified to adopt a look-through approach. ***Rather than treating shares or interests as active assets based on the activities of the underlying company, the modified test looks through such membership interests to include the proportionate amount of the value of the assets of other entities*** *(referred to as later entities) to which the interests ultimately relate'"*

Rationale for modified active asset test

- Modified active asset test seeks to prevent following:



- Carries on small marketing business as CGT small business entity
- Wishes to sell 20% share in Channel Investment Trust

- Owns assets of net market value of $2 million.
- $1.95 million consists of share/trust interests that do not exceed 10% in any other entity.

- Prior to 2018 changes, concessions may be available despite passive nature of investments by Channel investment Trust in unrelated businesses

Rationale for additional condition relating to taxpayer

- One basic condition requires that the taxpayer '*are a CGT small business entity **for the income year***'
- Additional condition of the taxpayer requires the taxpayer to '*generally have carried on business just prior to the CGT event happening. This ensures that entities do not benefit from this concession where the relevant business activities are too remote to justify the entity receiving a concession for business activities*'
- Does not apply where taxpayer satisfies MNAV test

Rationale for additional condition for Object Entity

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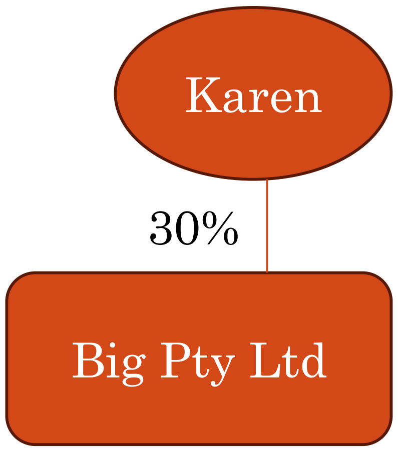
- The additional condition imposed on the Object Entity therefore sought to prevent '*the concession being available for interests in entities that are carrying on a business that is not a small business as it has both substantial aggregate turnover and net assets*'

Rationale for additional condition for Object Entity

- Additional condition for Object Entity seeks to prevent investment in large business accessing SBCGT concessions



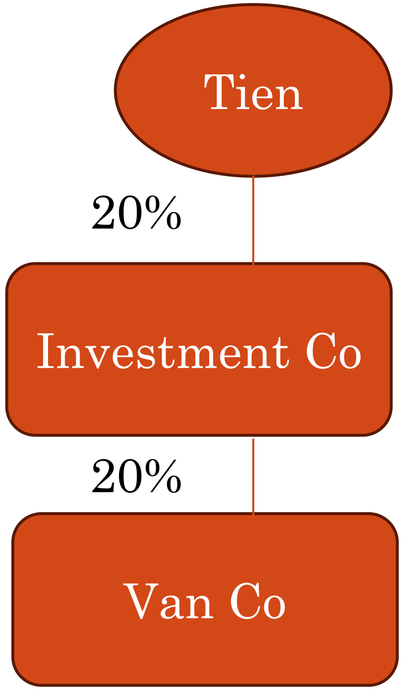
- Sole trader

- Large private company
- Annual turnover exceeding $20 million
- Assets exceeding $100 million

- Prior to 2018 changes, sale of Karen's shares could have accessed the SBCGT concessions as Big Pty Ltd would not have been considered connected with/affiliated with Karen and Karen would have been a CGT concession stakeholder.

Rationale for additional condition for Object Entity

- Additional condition for Object Entity seeks to prevent indirect investment in large business accessing SBCGT concessions



- Small business entity
- Transport company with turnover and assets exceeding Turnover and MNAV Tests

- Prior to 2018 changes, sale of shares by Investment Co may have been eligible for SBCGT concessions as Investment Co could have been considered a small business entity and turnover/assets of Van Co not included in tests

CGT concession stakeholder

- 152-10(2)(d) ITAA 1997 – CGT concession stakeholder test:

  (a) you are a CGT concession stakeholder in the object entity; or

  (b) CGT concession stakeholders in the object entity together have a small business participation percentage in you (the taxpayer) of at least 90%.

- 152-60 ITAA 1997 – meaning of CGT concession stakeholder :

  An individual is a CGT concession stakeholder of a company or trust at a time if the individual is:

  (a) a significant individual in the company or trust; or

  (b) a spouse of a significant individual in the company or trust, if the spouse has a small business participation in the company or trust at that time that is greater than zero.'

- 152-55 ITAA 1997 – meaning of significant individual:

  'An individual is a significant individual in a company or a trust at a time if, at that time, the individual has a small business participation percentages in the company or trust of at least 20%'.

Small business participation percentage

- 152-65 ITAA 1997 – how to calculate an entity's small business participation percentage:

  An entity's small business participation percentage in another entity at a time is the percentage that is the sum of:

  (a) the entity's direct small business participation percentage in the other entity at that time; and

  (b) the entity's indirect small business participation percentage in the other entity at that time.

Indirect small business participation percentage

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- 152-75 ITAA 1997 – how to calculate an entity's indirect small business participation percentage by multiplying:

  (1) Work out the indirect small business participation percentage that an entity (the holding entity) holds at a particular time in another entity (the test entity) by multiplying:

  (a) the holding entity's direct small business participation percentage (if any) in another entity (the intermediate entity) at that time; by

  (b) the sum of:

  (i) the intermediate entity's direct small business participation percentage (if any) in the test entity at that time; and

  (ii) the intermediate entity's indirect small business participation percentage (if any) in the test entity at that time (as worked out under one or more other applications of this section).

  (2) If there is more than one intermediate entity to which paragraph (1)(a) applies at that time, the holding entity's indirect small business participation percentage is the sum of the percentages worked out under subsection (1) in relation to each of those intermediate entities.

Indirect small business participation percentage

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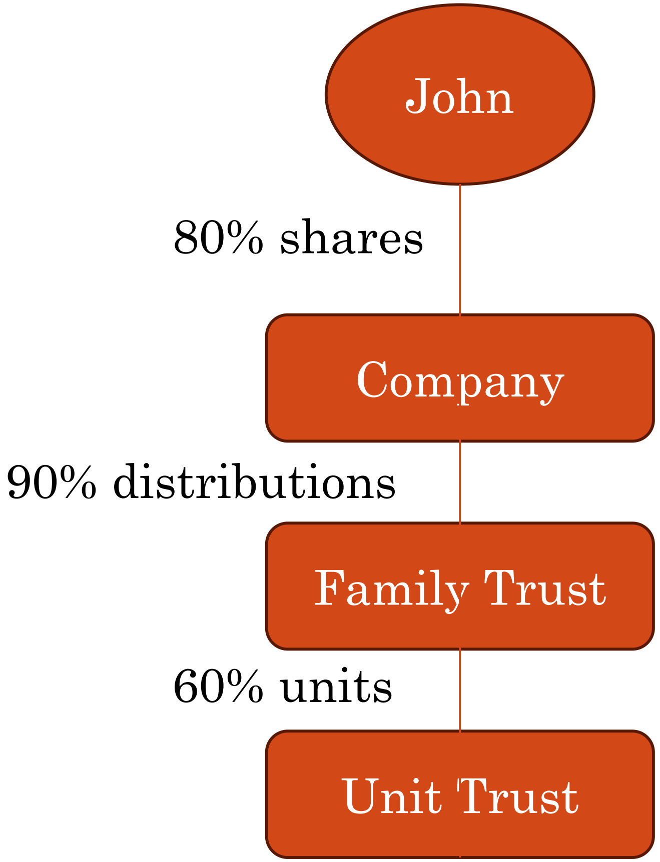

80% * 90% * 60% = 43.2% indirect small business participation percentage held by John in the Unit Trust

Direct small business participation percentage

- Different rules depending on type of entity set out in Table of 152-70(1) ITAA 1997:
  - Company
  - Trust (where entities do have entitlements to all the income and capital of the trust)
  - Trust (where entities do not have entitlements to all the income and capital of the trust)

Direct SBPP - company

This percentage that the entity has because of holding the legal and equitable interests in shares in the company:

(a) the percentage of the voting power in the company; or

(b) the percentage of any dividend that the company may pay; or

(c) the percentage of any distribution of capital that the company may make;

or, if they are different, the smaller or smallest.

Direct SBPP - company

- Different share classes on issue
  - Different rights
    - Dividend only
    - Voting only/founder shares

  Review company constitution and appropriate minutes

- Example:
  - A class shares – dividend and capital rights
  - B class shares – voting rights only

Class	Adam	Ben	Carol	David	Elaine
A	20%	20%	20%	30%	10%
B	35%	35%	20%	0%	10%
SBPP	**20%**	**20%**	**20%**	**0%**	**10%**

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Direct SBPP - company

- Employee share arrangements
  - Dividend access shares
  - Redeemable or not
- ATO TD 2006/77: *All classes of shares (other than redeemable shares) issued by a company are taken into account in determining if the company has a significant individual under section 152-55 of the Income Tax Assessment Act 1997 (ITAA 1997)*

Direct SBPP - company

- Examples from ATO TD 2006/77 – Example 1
  - Bedrock Co:
    - A class shares – distribution and voting rights – equally by Fred and Barney
    - B class shares – distribution rights only – equally by Wilma and Betty (spouses of Fred and Barney)
    - Directors can decide to distribute to one class of share over another
    - No shareholder has entitlement to any distribution so such percentage based on distribution is 0%
    - Even though Fred and Barney have a 50% percentage of voting rights, due to the smaller distribution right, their direct SBPP is taken to be the lesser

Class	Fred	Barney	Wilma	Betty
A	0%	0%	N/A	N/A
B	N/A	N/A	0%	0%
SBPP	**0%**	**0%**	**0%**	**0%**

Direct SBPP - company

- Examples from ATO TD 2006/77 – Example 3
  - A class shares held by owners – Gus holds 20% of the A class shares
  - 1 D class share issued to a key employee – dividend only payable at the discretion of directors
  - As Gus is not guaranteed to receive 20% of a distribution if the directors determines to declare a dividend to the D class shareholder, Gus is deemed to hold a lesser direct SBPP
  - Gus will not be a CGT concession stakeholder as he does not hold a 20% SBPP

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Direct SBPP - company

- Examples from ATO TD 2006/77 – Example 4
  - XYZ Co has 100 ordinary shares and 1 redeemable preference share
  - The redeemable share has voting rights equal to the ordinary share as well as preferential dividend right.
  - As the preference share is redeemable, it is ignored for the purposes of determining if XYZ Co has a significant individual.
  - Michelle holds 20 ordinary shares and would therefore be a significant individual of XYZ Co

Direct SBPP - company

- Review the terms of the share rights:

  "(i) any vote in respect of any such shares held by them at any meetings of the Company but shall be entitled to receive notice of such meetings and to attend thereat; or

  (ii) participate in a distribution of surplus assets (if any) remaining after payment of the amount paid up on all shares in the capital of the Company but shall be entitled to receive in respect of any such shares, such dividends, capital or other distributions (if any) other than on a winding-up as in respect of each class the Directors may from time to time determine to pay. The Directors may determine a dividend be paid on any one or more of such shares and any such declaration, payment or distribution shall be binding upon all members of the Company,

  provided that the holders have no right to payment of a dividend until such time as the directors of the company resolve that the holders of the shares have a right to payment of a dividend'.

Direct SBPP - company

- Bolded provision suggests ability to pay a dividend is not possible until active steps are taken.
- Bolded provision strongly than leaving dividend entitlements at the discretion of directors
- *Commissioner of Taxation v Devuba Pty Ltd* [2015] FCAFC 168

Direct SBPP – trust (all entitlements)

This percentage:

(a) the percentage of any distribution of income that the trustee may make to which the entity would be beneficially entitled; or

(b) the percentage of any distribution of capital that the trustee may make to which the entity would be beneficially entitled;

or, if they are different, the smaller.

Direct SBPP – trust (all entitlements)

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- Similar to companies – care should be taken to review terms of trust and rights of unit classes on issue
- ATO ID 2015/8: '*a trust instrument which gives the trustee discretion to appoint or distribute income or capital to one or more of a class of beneficiaries is a trust where entities do not have entitlements to all the income and capital of the trust. Although entities may become entitled to the income and capital of the trust as a result of the exercise of the trustee's discretion, those entitlements do not exist prior to that time*'

Direct SBPP – trust (no entitlements)

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This percentage:

(a) if the trustee makes distributions of income during the income year (the relevant year) in which that time occurs--the percentage of the distributions to which the entity was beneficially entitled; or

(b) if the trustee makes distributions of capital during the relevant year--the percentage of the distributions to which the entity was beneficially entitled;

or, if 2 different percentages are applicable, the smaller.

Direct SBPP – trust (no entitlements)

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- Related to direct SBPP in discretionary trust
- Due to discretionary nature, direct SBPP depends on the income and capital distribution on a year-on-year basis
- Care to be taken where recipients of income and capital distributions differ
- May arise when streaming and income definitions don't align

Beneficiary	Income%	Capital%	Direct SBPP
A	50%	0%	0%
B	50%	0%	0%
C	0%	100%	0%
SBPP	**0%**	**0%**	**0%**

Direct SBPP – trust (no entitlements)

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- ATO ID 2012/99 – 'distributions of income' and capital in the context of subsection 152-70(1) ITAA 1997

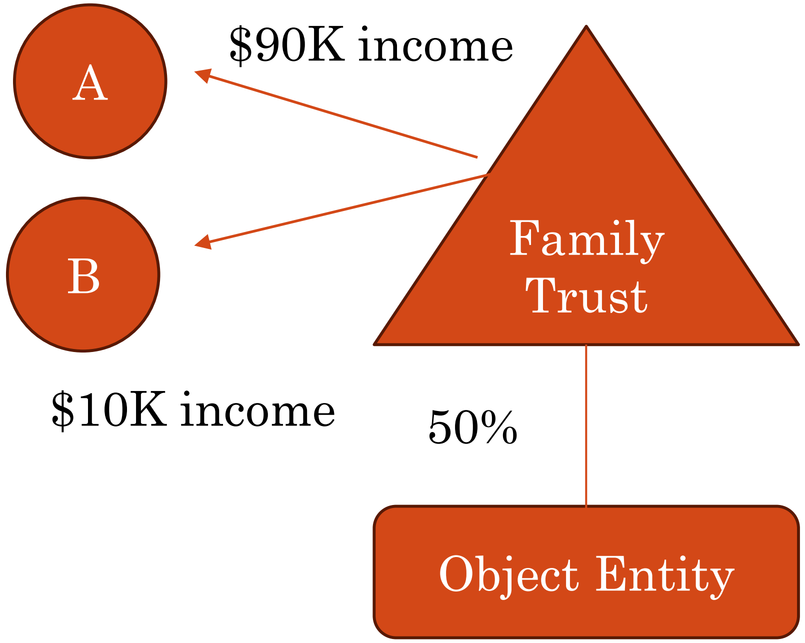
  'references to distributions of 'income' in the context of determining an entity's direct small business participation percentage in a trust mean the income of the trust, determined according to the general law of trusts, to which a beneficiary could be entitled. Depending on the deed and/or actions of the trustee, this may be an amount that differs from the ordinary income of the trust'

- Consider definition of income:
  - Ordinary meaning – streaming capital gains made under capital distribution power
  - Section 95 income – sheltered capital gains may require streaming under capital distribution power
  - Recharacterisation power – no capital distribution required and no lesser amount an issue
  - TR 2012/D1 – what can and cannot be income (i.e. notional amounts)

Direct SBPP – trust (no entitlements)

- Care that 0% percentages may be deemed where:
  - Trust has net income and did not have a tax loss and no distributions made; or
  - Trust has not made an income or capital distribution in its history

Direct SBPP – trust (no entitlements)



- Capital gain of $90,000
- Trust deed contains power to determine whether receipts are on capital or revenue account
- Trustee determines capital gain to be held on revenue account
- $10,000 additional ordinary income
- No capital distribution made
- A's indirect SBPP in Object Entity = 90% ($90,000/$100,000) * 50% = 45%
- B's indirect SBPP in Object Entity = 5%

Modified active asset test

- Requires understanding of the general active asset test, particularly regarding where CGT asset is an interest in an Object Entity
- General test requires active asset held for either:
  - half the total period held; or
  - if held for more than 15 years, at least 7.5 years
- Where CGT asset is an interest in an Object Entity – section 152-40(3) ITAA 1997 includes requirement that total:
  - the market values of the active assets of the Object Entity; and
  - the market value of any financial instruments of the Object Entity that are inherently connected with a business that the Object Entity carries on; and
  - any cash of the Object Entity that is inherently connected with such a business;

  is 80% or more of the market value of all of the assets of the Object Entity

General active asset test

- Impractical to undertake a day-to-day review, section 152-40(3A) ITAA 1997 allows deemed satisfaction where '*it is reasonable to conclude that the share or interest is still an active asset at the later time*'
- Does require understanding of balance sheet of Object Entity
  - Consider whether excess cash in business 'inherently connected' and can be explained
  - Consider financial instruments (which includes loans and other investments) if they are 'inherently connected' with business
  - Consider assets that are a permanent or characteristic attribute of the business (goodwill/trade debtors)
- Traps include (but are not limited to):
  - Loans to related entities to acquire investments
  - Excess cash used to acquire share investments in trading entity

General active asset test

- Where Object Entity owns an interest in a later entity, 80% active asset test applied at each successive level
- TD 2006/65 at paragraphs 15 and 16:

'15 If an entity owns a share in a company or interest in a trust that is an active asset because the company or trust satisfies the '80% test', the share or interest is included in that entity's '80% test' calculation to determine if the underlying interests in the entity are themselves active assets.

16. As the active asset test requires a CGT asset to be an active asset for at least half a particular period (generally the ownership period), the '80% test' must also be satisfied for that same period for a share in a company or interest in a trust to satisfy the active asset test.'

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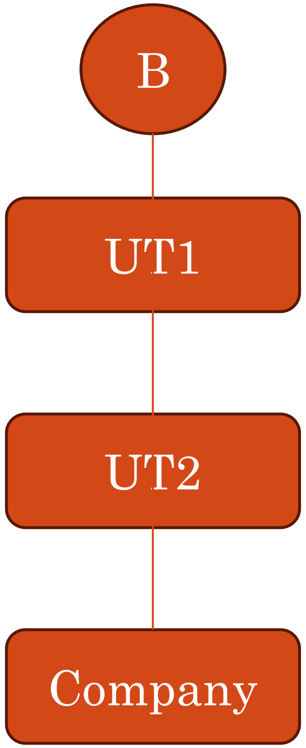
General active asset test



- Bill owns all units in Unit Trust 1
- Unit Trust 1 owns all units in Unit Trust 2
- Unit Trust 2 owns all shares in Company 1
- All assets in Unit Trust 2 are active assets other than shares in Company (market value of Company shares relative to Unit Trust 2 total assets is 15%)
- Company owns an active asset with a market value relative to Company total assets of 50%
- As Company does not have market value of active assets of at least 80%, the shares in the Company will not be active assets
- As all other assets of Unit Trust 2 are active, the 80% test is satisfied.
- Accordingly, all Unit Trust 1 assets are active as well

Modified active asset test

- 152-10(2A) ITAA 1997 (referred to in 152-10(2)(a) ITAA 1997):

(2A) For the purposes of paragraph (2)(a), in working out whether subsection 152-40(3) applies at a given time (the test time) assume that:

(a) an asset of a company or trust is covered by neither:

(i) subparagraph 152-40(3)(b)(ii) (about financial instruments); nor

(ii) subparagraph 152-40(3)(b)(iii) (about cash);

if the company or trust acquired that asset for a purpose that included assisting an entity to otherwise satisfy paragraph (2)(a) of this section; and

(b) paragraph 152-40(3)(b) does not cover an asset that:

(i) is a share in a company, or an interest in a trust, (the later entity); and

(ii) is held at the test time by the object entity directly or indirectly (through one or more interposed entities); and

Modified active asset test

- 152-10(2A) ITAA 1997 (referred to in 152-10(2)(a) ITAA 1997) cont:

  …(c) subparagraph 152-40(3)(b)(i) also covers each asset that:

  (i) is held at the test time by a later entity covered by subsection (2B); and

  (ii) is, for that later entity, an asset of a kind referred to in subparagraph 152-40(3)(b)(i), (ii) or (iii), as modified by paragraphs (a) and (b) of this subsection; and

  (d) subject to paragraph (b) of this subsection, all of the assets of the object entity at the test time included all of the assets of each later entity at the test time; and

  (e) for the purposes of paragraph 152-40(3)(b), the market value at the test time of an asset held by a later entity were the product of:

  (i) the asset's market value, apart from this paragraph, at the test time; and

  (ii) the object entity's small business participation percentage in the later entity at the test time.

Modified active asset test

- Modification 1 – financial instruments and cash (referred to in subsections 152-40(3)(b)(ii) and (iii) ITAA 1997) are not included in the active asset calculation if they are acquired with a purpose to only meet the active asset test;
- Modification 2 – a share or interest held by the Object Entity in a company or trust (the later entity) are not included in the calculation of the Object Entity's active asset;
- Modification 3 – the Object Entity's active assets include the market value of:
  - assets owned by later entities covered under section 152-10(2B) ITAA 1997; and
  - active assets of those later entities are those provided for in section 152-40(3)(B) ITAA 1997 as modified under the above;

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Modified active asset test

- Modification 4 – other than in relation to requirement 2, all assets of later entities are considered assets of the Object Entity (i.e. the assets of the later entities are included in the active asset test but not the shares and units the Object Entity holds in those later entities);
- Modification 5 – the market value of assets held by the Object Entity in later entities is the product of the asset's market value and the Object Entity's small business participation percentage in the later entity.

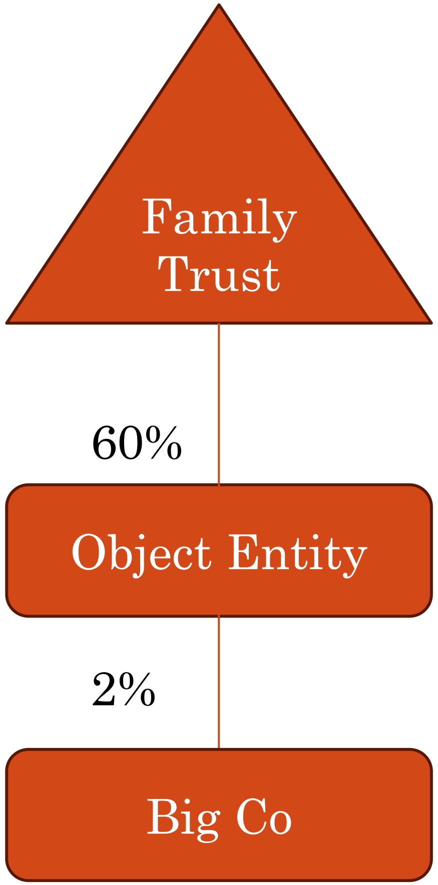
Modified active asset test

- In relation to Modification 3, the market value of the active assets of the following later entities are included in the Object Entity test:
  - later entities where the taxpayer of the Object Entity has a small business participation percentage in the later entity of at least 20% or the taxpayer is a CGT concession stakeholder of the later entity;
  - the later entity is a small business CGT entity or satisfies the MNAV test on the following basis:
    - the only CGT assets or annual turnovers considered were those of the later entity, the Object Entity, each affiliate of the Object Entity, and each entity controlled by the Object Entity in a way described in section 328-125 ITAA 1997;
    - each reference in section 328- 125 ITAA 1997 to 40% were a reference to 20%

Modified active asset test

- Practical implication on reviewing financial information of later entities
- More work required upfront to understand position prior to CGT event

Modified active asset test example



- Object Entity:
  - Active Assets - $2m
  - Turnover - $1m
  - Object Entity market value in Big Co - $1m
- Big Co:
  - Net Assets - $50m
  - Turnover $50m

Modified active asset test example 1

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- Modification 1 - Ignore all cash and financial instruments that were only obtained to satisfy the active asset test – Assume none
- Modification 2 – Ignore value of shares Object Entity holds in later entities
- Modification 3 – Run active asset test for Object Entity and only consider active assets for later entities:
  - where taxpayer holds 20% SBPP or is a CGT concession stakeholder; and
  - who meets the MNAV or Turnover Test

  Include $2m active assets in Object Entity but as Object Entity not a CGT concession stakeholder in Big Co, ignore active assets in Big Co
- Modification 4 and 5 – Apportion Object Entity's interest in Big Co - $1m (2% of $50m)
- Modified active asset test - $2m/$3m = 66.66% - Shares in Object Entity not active

Modified active asset test example – variation A

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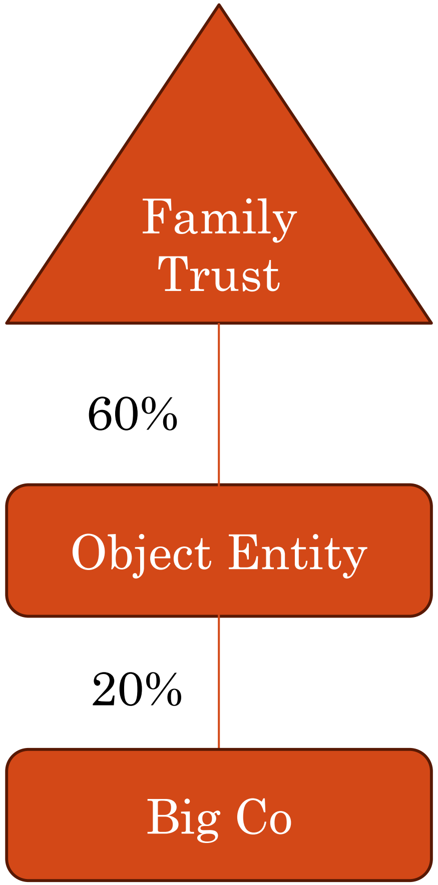

Modified active asset test still fails as Big Co active assets not included as Big Co does not meet MNAV/Turnover Test

- Object Entity:
  - Active Assets - $2m
  - Turnover - $1m
  - Object Entity market value in Big Co - $1m
- Big Co:
  - Net Assets - $50m
  - Turnover $50m

Modified active asset test example – variation B

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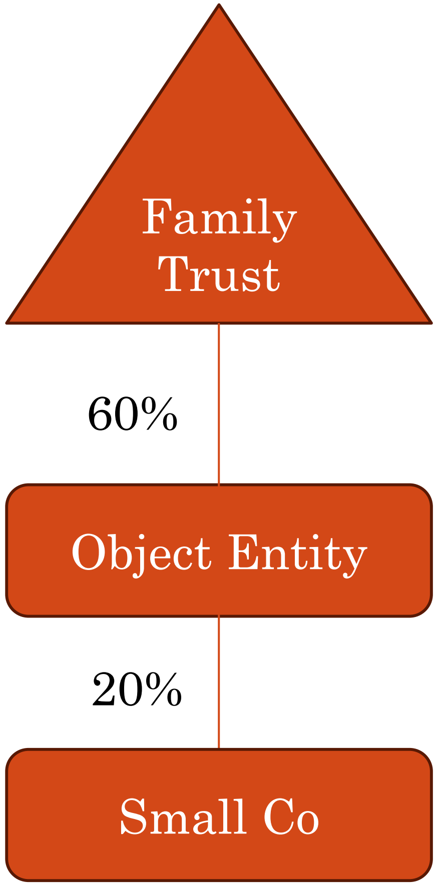
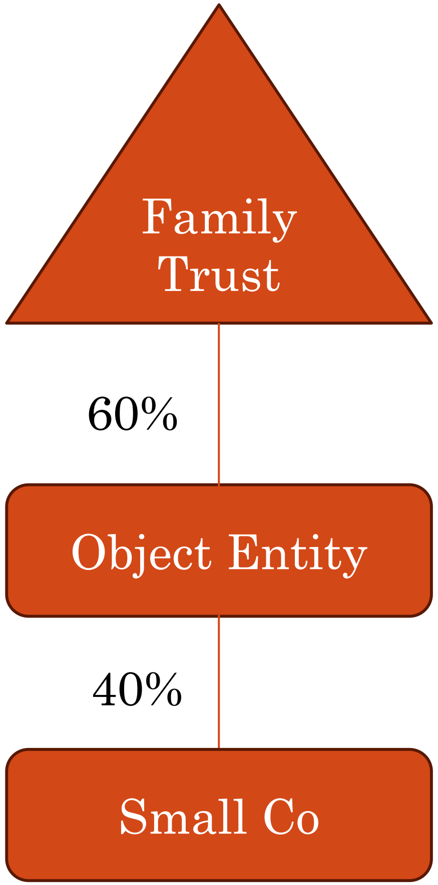


Modified active asset test still fails as although Small Co meets MNAV/Turnover Test, there is no person who can obtain a 20% small business participation percentage in Small Co, so assets of Small Co not active

- Object Entity:
  - Active Assets - $2m
  - Turnover - $1m
  - Object Entity market value in Big Co - $1m
- Small Co:
  - Active and Net Assets - $1m
  - Turnover $1m

Modified active asset test example – variation C



Modified active asset test may be met as assets of Small Co included in calculation of active assets for Object Entity (as it is possible for a person to obtain a 20% small business participation percentage in Small Co and Small Co satisfies the MNAV/Turnover test)

- Object Entity:
  - Active Assets - $2m
  - Turnover - $1m
  - Object Entity market value in Big Co - $1m
- Small Co:
  - Active and Net Assets - $1m
  - Turnover $1m

Additional condition relating to taxpayer

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- 152-10(2)(b) ITAA 1997:

  (b) if you do not satisfy the maximum net asset value test (see section 152-15)--you are carrying on a business just before the CGT event;

- Non-contentious

- Where taxpayer not carrying on a business just before the CGT event – taxpayer required to meet the MNAV test

Additional condition relating to Object Entity

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- 152-10(2)(c) ITAA 1997:

  (c) either:

  (i) the object entity would be a CGT small business entity for the income year; or

  (ii) the object entity would satisfy the maximum net asset value test (see section 152-15);

  if the following assumptions were made:

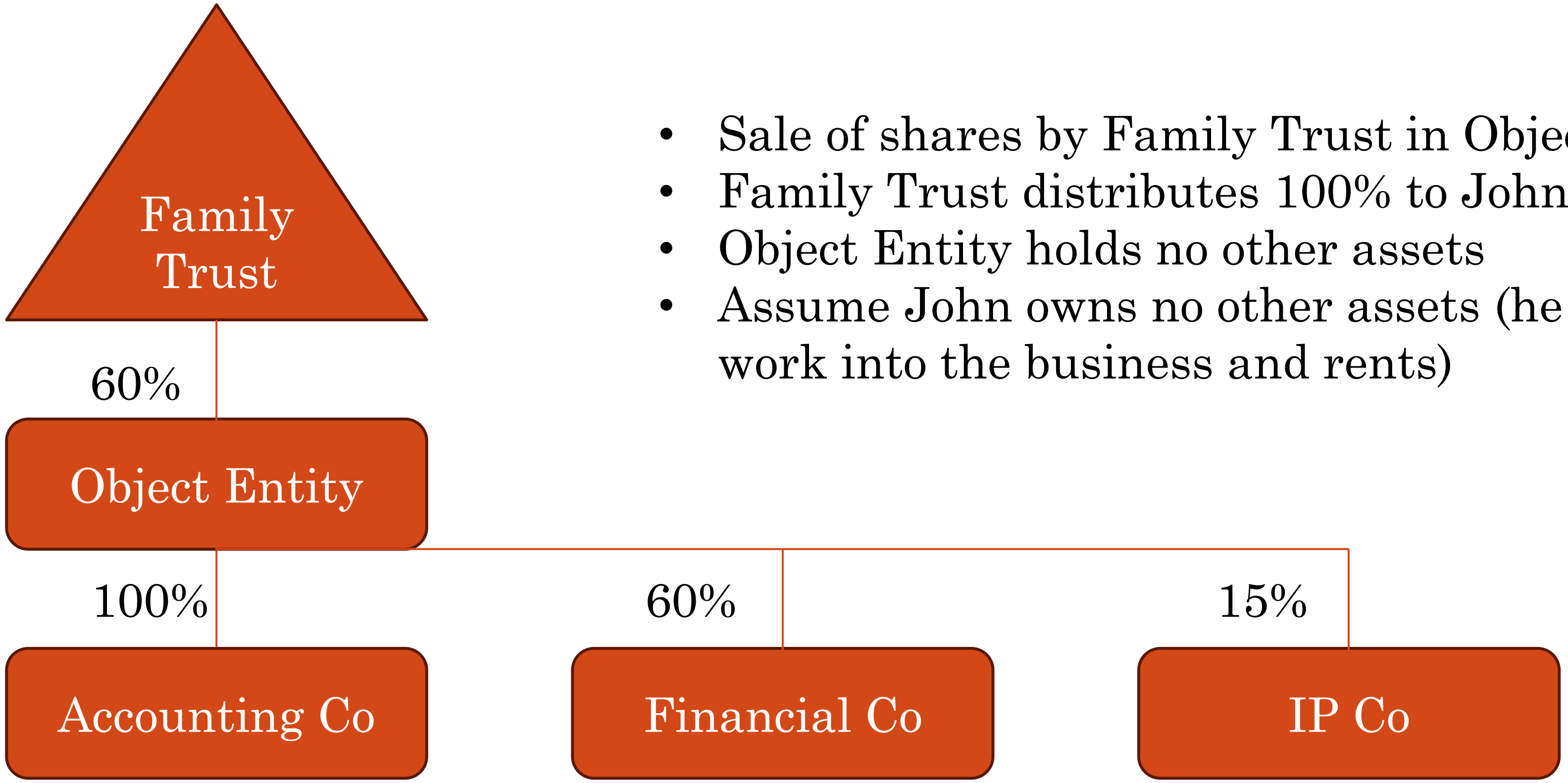
  (iii) the only CGT assets or annual turnovers considered were those of the object entity, each affiliate of the object entity, and each entity controlled by the object entity in a way described in section 328- 125;

  (iv) each reference in section 328- 125 to 40% were a reference to 20%;

  (v) no determination under subsection 328-125(6) were in force;

- Rerunning a modified MNAV/Turnover Test at the Object Entity level noting:
  - connected entity threshold reduced to 20%
  - only include connected entities **controlled by** Object Entity

Example 1



- Sale of shares by Family Trust in Object Entity
- Family Trust distributes 100% to John
- Object Entity holds no other assets
- Assume John owns no other assets (he put his life's work into the business and rents)

\$1m	\$0.5m	\$0.1m	**Turnover**
\$1m	\$4m	\$10m	**Assets**

Example 1 – Modified active asset test

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- Modification 1 - Ignore all cash and financial instruments that were only obtained to satisfy the active asset test – Assume none
- Modification 2 – Ignore value of shares Object Entity holds in later entities
- Modification 3 – Run active asset test for Object Entity and only consider active assets for later entities who have a CGT concession stakeholder and meets the MNAV or Turnover Test
  - Family Trust interest in Accounting Co is 60% (60% * 100%) so include active assets in Accounting Co
  - Family Trust interest in Financial Co is 36% (60% * 60%) so include active assets in Financial Co
  - Family Trust interest in IP Co is 9% (60% * 15%) so do not include active assets in IP Co

Example 1 – Modified active asset test

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- Modification 4 and 5 – Apportion Object Entity's interest in each later entity's active assets:
  - Accounting Co – 100% * $1m = $1m active assets
  - Financial Co – 60% * $4m = $2.4m active assets
- Total assets in Object Entity =
  - No other assets in Object Entity
  - Accounting Co = $1m
  - Financial Co = $2.4m
  - IP Co = $1.5m (15% * $10m)
- Active assets in Object Entity = $3.4m/$4.9m = 69.38% = Shares in Object Entity not active

Example 1 – Modified active asset test

- *Assume total assets in IP Co is $5m (instead of $15m), meaning Object Entity non-active asset value in IP Co is $500,000 (10% * $5m)
- $3.4m/$3.9m = 87.18%
- Modified active asset test passed

Additional condition relating to taxpayer

- As the Family Trust does not carry on a business, consider if MNAV Test met
- Assuming John has no other assets, then entities connected with Family Trust include Accounting Co
- Net assets less than $6m

Additional condition relating to Object Entity

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- Rerunning a modified MNAV/Turnover Test at the Object Entity level noting:
  - connected entity threshold reduced to 20%
  - only include connected entities **controlled by** Object Entity
- In relation to Object Entity:
  - Accounting Co and Financial Co assets are included in rerun MNAV Test
  - IP Co assets not included as Object Entity does not hold at least a 20% interest in IP Co
  - Total net assets of Object Entity, Accounting Co and Financial Co:
    - Accounting Co - $1m
    - Financial Co - $4m
    - Object Entity – ignore shares in Accounting Co and Financial Co but include value of shares in IP Co
  - Rerun MNAV test may fail if IP Co assets valued at $10m (causing shares to be valued at $1.5m), but may be satisfied if valued lower (per prior variation)

CGT concession stakeholder

- John holds a small business participation percentage in Object Entity of 60% (as he received 100% of the income distributions, no capital distributions made)
- Had the trust distributions been split equally between John and his wife, there would still be a CGT concession stakeholder as they would each hold a 30% small business participation percentage

Final thoughts

- Additional conditions get complicated when there are layers of entities involved
- Even in simple scenarios, where trading entities hold interests in other 'later entities', can cause a layer of complexity
- Pre-planning required as some of the additional conditions rely on one's small business participation percentage – which is complicated when discretionary trusts are involved in the chain

Contact details

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